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IN THE

Supreme Court of the United States

OCTOBER TERM, 1956

No. 258

AMERICAN WELL AND PROSPECTING COMPANY,

Petitioner,

against

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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July 12, 1956.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1956

AMERICAN WELL AND PROSPECTING COMPANY, *Petitioner,* *against* COMMISSIONER OF INTERNAL REVENUE, *Respondent.*	No. .....

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

To the Honorable The Chief Justice of the United States and the Associate Justices of the Supreme Court of the United States:

Your petitioner, American Well and Prospecting Company, a Texas corporation, respectfully prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Third Circuit entered March 22, 1956, which affirmed a decision of The Tax Court of the United States. A certified transcript of the record is furnished herewith in accordance with Rule 21, Pars. 1 and 3, of the Rules of this Court.

Opinions Below

The opinion of the Tax Court (R. 3a)* is reported in 23 T. C. 503. The opinion of the Court of Appeals (a

*Nine additional copies of the printed Appendix for the petitioner in the Court of Appeals are furnished herewith in accordance with Rule 21, Pars. 3 and 4, of the Rules of this Court. The record references are to that Appendix.

copy of which is appended to this petition as Exhibit A) is reported in 232 F. 2d 934.

Jurisdiction

The judgment of the Court of Appeals (a copy of which is appended to this petition as Exhibit B) is dated March 22, 1956, and was entered on that date. A petition for rehearing which was filed with the Court of Appeals on April 5, 1956, was denied on April 18, 1956. A copy of the order of denial is appended to this petition as Exhibit C. The jurisdiction of this Court is invoked under Title 28, United States Code, Judiciary and Judicial Procedure, Section 1254 (62 Stat. 928).

Questions Presented

1. If the petitioner, a Texas corporation, was in existence during 1946 (as found by the Tax Court), is it entitled to carry back to 1944 its unused excess profits credit for 1946 in the amount of $74,909.27 under the provisions of Section 710(c)(3)(A) of the Internal Revenue Code of 1939, although in 1946 it was not engaged in the business which produced its 1944 income against which the carry-back to 1944 would be applied?

2. Was the finding of the Court of Appeals that the petitioner was *de facto* dissolved and hence did not have any existence for Federal tax purposes in 1946 a proper one, particularly in view of the finding of fact by the Tax Court that the petitioner remained in existence in 1946 for a proper business purpose?

Statutes and Regulations Involved

The pertinent provisions of the statute and the regulations, namely, Section 710(b)(3), Section 710(c) and Section 712(a) of the Internal Revenue Code of 1939, Section 29.52-1 of Treasury Regulations 111, and Section 35.710-3(a) of Treasury Regulations 112, are printed in the Appendix, *infra*.

Statement

The facts were stipulated (R. 12a-18a) and may be summarized as follows:

The petitioner is a corporation organized in 1931 under the laws of Texas and is existing and presently engaged in business (R. 12a, 18a).

In 1931 through 1945, the petitioner was engaged in the business of manufacturing and selling oil well equipment and also in the manufacture of armaments for the United States Government (R. 13a). Since 1944, all the petitioner's outstanding stock has been owned by Bethlehem Steel Company, a Pennsylvania corporation, all the stock of which in turn has been owned by Bethlehem Steel Corporation, a Delaware corporation (R. 13a).

The petitioner's business was operated at a loss in 1945 (Exhibit 3-C).

As of the opening of business on January 1, 1946, the petitioner sold all its transferable property, assets and business for approximately $900,000 to Bethlehem Supply Company, a Delaware corporation, which was also engaged in the manufacture and sale of oil well equipment (R. 4a, 13a). The petitioner also agreed to collect its non-assignable assets and turn over the proceeds to Bethlehem Supply Company (R. 5a, 24a). All the outstanding stock of Bethlehem Supply Company was and is owned by Bethlehem Steel Corporation (R. 14a).

Among the non-assignable assets owned by the petitioner were certain claims against the United States in the amount of approximately $300,000 (R. 4a, 13a). The major part of those claims was collected in May and August of 1946 (R. 6a, 15a, 16a). A further claim of approximately $25,000 had not been collected at the time of the hearing (R. 6a, 16a). The Tax Court found that the petitioner on January 1, 1946, "ceased to operate a business but remained in existence to cooperate with the purchaser [of its assets] so that the latter might derive the benefit of certain contracts and claims that were unassignable" (R. 3a).

During 1946 and 1947, the petitioner was also engaged in settling claims by the United States against it (R. 16a); in purchasing and disposing of certain material and machinery owned by the United States, but located upon the property formerly owned by the petitioner (R. 16a); and in defending a suit for $219,000 brought against the petitioner in June, 1946, by a former employee which was not disposed of until 1948 (R. 17a).

The petitioner retained the $900,000 proceeds of the sale of its assets during the entire taxable years 1946 and 1947. It never made any liquidating distributions to its shareholders (R. 8a). No proceedings to dissolve the petitioner were taken (R. 15a).

The petitioner filed Federal income tax returns for 1946 and 1947 (Exhibits 4-D and 5-E).

Annual meetings of the petitioner's stockholders and meetings of its directors were held in 1946 and 1947 (R. 27a-47a).

In 1948, the petitioner invested part of the proceeds of the sale of its business in a drydock and has since been in the business of renting the drydock (R. 17a, 18a).

The jurisdiction of The Tax Court of the United States is based upon Section 272(a)(1) of the Internal Revenue Code of 1939.

Section 710(c)(3)(A) of the Internal Revenue Code of 1939 (set forth in the Appendix to this petition) provides that if a taxpayer has an unused excess profits credit for 1946, such unused credit "shall be an unused excess profits credit carry-back for each of the two preceding taxable years", in this case 1944 and 1945. The amount of the petitioner's unused excess profits credit for 1946 is not in dispute (R. 18a).

The Tax Court held that the petitioner was not entitled to a carry-back of unused excess profits credit from 1946 to 1944 on the ground that the petitioner was not engaged in 1946 in the business which produced the 1944 profits against which the carry-back of unused credit for 1946 was to be applied. In such a case the Tax Court held that the Congress did not intend to permit a carry-back (R. 10a). The Tax Court, however, expressly found that the petitioner "remained in existence" in 1946 in order to collect its unassignable claims (R. 3a).

The Court of Appeals affirmed the decision of the Tax Court, but upon the ground that the petitioner was not in existence during 1946, since it had been *de facto* dissolved in January, 1946 (pp. 6, 9).* In so doing, the Court of Appeals found (contrary to the finding of the Tax Court) that there was no business reason for continuing the petitioner's existence in 1946 (p. 9).

Reasons for Granting the Writ

1. The Court of Appeals has rendered a decision in conflict with the decisions of other Courts of Appeals on the same matter, namely, *Diamond A Cattle Co. v. Commissioner*, 50-2 USTC par. 9629 (10th Cir. May 17, 1950,

*References are to the opinion of the Court of Appeals (Exhibit A to this petition).

not yet officially reported), reversing 21 T. C. 1 (1953);* *Wier Long Leaf Lumber Co.* v. *Commissioner*, 173 F. 2d 549 (5th Cir. 1949) [as to the year 1943], reversing 9 T. C. 990 (1947); and *Boxman* v. *Glenn*, 84 F. Supp. 200 (W. D. Ky. 1949), *aff'd* 184 F. 2d 670 (6th Cir. 1950). Those decisions in the Tenth, Fifth and Sixth Circuits involved the exact question presented by the instant case, namely, whether a corporation which has disposed of the business from which it made profits in prior years can carry back to offset income of prior years in which the business was operated an unused excess profits credit for a period after it disposed of the business. Those three Courts of Appeals held that the carry-back provision was mandatory. They allowed the carry-back even though the corporations involved were avowedly in the process of liquidation. The business reasons for the continuation of the petitioner's existence in 1946 were at least as great as the reasons for the continued existence of the corporations involved in those three cases during the years from which carry-backs were permitted, and in which the corporations were held to be in existence and not to have been *de facto* dissolved.

2. This case presents a question of large and continuing importance in the functioning of the Federal tax laws which has not been, but should be, settled by this Court. That question is: When does a corporate taxpayer cease to be in existence for the purposes of the Federal tax laws? The question has been the subject of considerable litigation and has arisen in a number of different forms.

(a) One form which the question has taken is whether a corporation's existence has been terminated

*The Tax Court opinion in the *Diamond A Cattle Co.* case was written by the author of the Tax Court opinion in the instant case and is identical in reasoning with the latter opinion.

so as to bar its right to a carry-back of unused excess profits credit (the precise point involved in this case). The large number of cases in which the question has been litigated shows its importance.*

(b) Another form which the question has taken is whether a corporation's existence has been terminated during the period of its liquidation so as to bar its right to a carry-back of operating losses. *Acampo Winery & Distilleries, Inc.*, 7 T. C. 629, 639-40 (1946); and *Gorman Lumber Sales Co.*, 12 T. C. 1184, 1194 (1949), *supra*. Those cases hold that an operating loss of a liquidating corporation which has disposed of all its business assets that produced the income in prior years may be carried back to offset the income of those prior years.

(c) A further form which the question has taken is whether a corporation's existence has ceased for the purpose of terminating the taxable year. That question has been litigated in several cases with a result generally in conflict with the decision of the Court of Appeals in the instant case: *United States* v. *Kingman*, 170 F. 2d

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*In addition to the three cases previously cited, the question has also been litigated with varying results in the following cases: *A B C Brewing Corp.* v. *Commissioner*, 224 F. 2d 483 (9th Cir. 1955); *Jos. Capps, Inc.* v. *United States*, 86 F. Supp. 712 (S. D. Cal. 1949); *Eastern Grain Elevator Corp.* v. *McGowan*, 95 F. Supp. 40 (W. D. N. Y. 1950); *Justice Motor Corp.* v. *McGowan*, 97 F. Supp. 570 (W. D. N. Y. 1951); *Westover Co.* v. *Smyth*, 99 F. Supp. 488 (N. D. Cal. 1951) [for opinion see 51-2 USTC par. 66,019]; *Myers* v. *United States*, 52-1 USTC par. 66,031 (E. D. Ark. 1952); *Brainard* v. *Scofield*, 140 F. Supp. 754 (W. D. Tex. 1953); *Arizona Concrete Company* v. *Stuart*, 55-2 USTC par. 9545 (D. Ariz. 1955); *Rite-Way Products, Inc.*, 12 T. C. 475 (1949); *Gorman Lumber Sales Co.*, 12 T. C. 1184 (1949); *Winter & Company, Inc. (Indiana)*, 13 T. C. 108 (1949); *Whitney Manufacturing Co.*, 14 T. C. 1217 (1950); *Coca Cola Bottling Co.*, 19 T. C. 282 (1952); *Wheeler Insulated Wire Co., Inc.*, 22 T. C. 380 (1954); *cf. Aluminum Products Company* v. *United States*, 101 F. Supp. 373 (Ct. Cls. 1951).

408 (5th Cir. 1948); *Union Bus Terminal* v. *Commissioner*, 179 F. 2d 399 (5th Cir. 1950), affirming 12 T. C. 197 (1949); and *Commissioner* v. *Allegheny Broadcasting Corporation*, 179 F. 2d 844 (3rd Cir. 1950). Here again the Courts of Appeals have held that corporations with no more activity than that of the petitioner in 1946 in the instant case were not *de facto* dissolved so as to end their existence for Federal tax purposes.

(d) Still another form which the question has taken is whether a corporation's existence has been terminated so that an excess profits credit may not be used for later years, or operating losses of prior years may not be carried forward against income of later years, where there is an intervening period of comparative inactivity. *Great American Industries, Inc.*, 25 T. C. No. 133 (March 8, 1956); *Alprosa Watch Corporation*, 11 T. C. 240 (1948); *W A G E, Inc.*, 19 T. C. 249 (1952); *A. B. & Container Corporation*, 14 T. C. 842 (1950). See also *Mesaba-Cliffs Mining Co.* v. *Commissioner*, 174 F. 2d 857 (6th Cir. 1949). Here again the rationale of the cases is contrary to the decision of the Court of Appeals in the instant case.

(e) Another form which the question has taken is whether a corporation's existence has terminated for the purpose of determining whether it should have filed a return and whether certain income is taxable to it or to its shareholders. The Treasury Regulations have for many years provided that a corporation is in existence for Federal tax purposes and is required to file Federal income tax returns even though it ceases business and dissolves (whether *de facto* or *de jure*), if it retains valuable assets or claims. Thus, Section 29.52-1 of Treasury Regulations 111, effective during 1946, provides as follows:

> " . . . A corporation is not in existence after it ceases business and dissolves, *retaining no assets,* whether or not under State law it may thereafter be treated as continuing as a corporation for certain limited purposes connected with winding up its affairs, such as for the purpose of suing and being sued. If the corporation has valuable *claims* for which it will bring suit during this period, *it has retained assets, and it continues in existence. . . .*" (Emphasis added.)

Following that regulation, it has been held that a dissolved corporation which was engaged in liquidating its assets is still a "corporation" within the meaning of the Federal tax laws and is required to file returns and pay taxes. *O'Sullivan Rubber Company (in Dissolution)* v. *Commissioner*, 120 F. 2d 845 (2nd Cir. 1941). That regulation and the cases construing it are contrary to the decision of the Court of Appeals in the instant case.

3. The Court of Appeals in rendering its decision has so far departed from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision.

When the petitioner on January 2, 1946, sold all its assignable assets to Bethlehem Supply Company, it had other assets in the form of claims against the United States which, because of the provision of 10 Stat. 170, as amended (Section 203, Title 31, United States Code), were not assignable; assignment of them rendered them absolutely void.* Accordingly, the petitioner agreed to collect the non-

*The relevant part of 10 Stat. 170, as amended, Section 203, Title 31, United States Code, reads as follows:

> "All transfers and assignments made of any claim upon the United States, or of any part or share thereof, or interest therein, whether absolute or conditional, and whatever may be the consideration therefor, and all powers of attorney, orders,

assignable claims which had arisen in its business and, when it had finished collecting them, to transfer the proceeds thereof to Bethlehem Supply Company. The problem of collecting non-assignable claims arises on a sale to a third party, such as Bethlehem Supply Company (*United States* v. *Shannon*, 342 U. S. 288 (1952)). If the petitioner had sold those claims to Bethlehem Supply Company on January 2, 1946, they would have become void. The petitioner had not finished collecting such unassignable claims by the end of 1946 (R. 13a, 16a, 17a, 24a).

The Tax Court found that the petitioner

> "remained in existence to cooperate with the purchaser [of its assets] so that the latter might derive the benefit of certain contracts and claims that were unassignable." (R. 3a)

The Commissioner of Internal Revenue accepted that finding in his brief which he filed with the Court of Appeals and incorporated it in his statement of the question involved on the appeal pursuant to Rule 24(2)(b) of the Rules of that Court, stating that the petitioner

> "remained in existence to cooperate with the purchaser so that the latter might derive the benefit of certain contracts and claims that were unassignable." (Br., p. 2)

The Tax Court's finding of fact that the petitioner remained in existence for the business purpose of cooperating with the purchaser of its assets in connection with the collection of non-assignable claims is supported by substantial evidence. The Tax Court found that the petitioner had

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or other authorities for receiving payment of any such claim, or of any part or share, thereof, shall be absolutely null and void, unless they are freely made and executed in the presence of at least two attesting witnesses, after the allowance of such a claim, the ascertainment of the amount due, and the issuing of a warrant for the payment thereof. * * *"

claims against the United States, which arose out of the business it had formerly conducted, in the amount of approximately $300,000 (R. 6a). If the petitioner had sold them to Bethlehem Supply Company, they would have, under decisions of this Court, become void. The collection of non-assignable claims arising out of its business which it owned and which only it could collect was a part of the orderly winding up of the petitioner's affairs. Certainly, counsel for the petitioner could not properly have advised that the petitioner be dissolved prior to the collection of the non-assignable claims against the United States. Prior to the time all those claims were collected, the petitioner was actively engaged in another business.

The Court of Appeals disregarded the finding of the Tax Court that the petitioner remained in existence for a proper business purpose. The holding of the Court of Appeals is summed up in the following two sentences in its opinion (p. 9):

> "In any event, there could be only two reasons for keeping a corporation alive under the circumstances of the case at bar in 1946: to avoid taxes, or to have a spare corporate charter conveniently ready for use whenever desired by the parent corporation. Neither is a sufficient business purpose of the taxpayer to negate the Tax Court's finding that the taxpayer in the case at bar was not entitled to an unused excess profits credit carry-back from the tax year 1946."

The extent to which the Court of Appeals disregarded the finding of the Tax Court is also shown by the way in which it attempted to distinguish the cases relied upon by the petitioner as supporting the allowance of the carry-back. The Court of Appeals distinguished those cases on the ground that "the taxpayers involved were much more than corporate shells kept alive only for purposes of tax

evasion" (p. 8). As stated above, the Tax Court found that the petitioner was continued in existence for a proper business purpose and the statement by the Court of Appeals in its opinion that the petitioner was kept alive in 1946 for purposes of tax evasion was not even suggested by the Commissioner of Internal Revenue at any stage in the proceeding and is entirely unsupported in the record.

The disregard by the Court of Appeals of the proper business reason why the petitioner remained in existence during 1946, as found by the Tax Court, is such a departure from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision. *Commissioner* v. *Scottish American Investment Co., Ltd.*, 323 U. S. 119, 123-124 (1944). See also *Choate* v. *Commissioner*, 324 U. S. 1 (1945); *Wilmington Trust Co.* v. *Helvering*, 316 U. S. 164 (1942); *Helvering* v. *Kehoe*, 309 U. S. 277 (1940); and *Helvering* v. *F. & R. Lazarus & Co.*, 308 U. S. 252 (1939). That the Tax Court's finding was based on stipulated facts does not change the rule that it is an abuse of the power of appellate review to ignore the Tax Court's findings of fact. *Boehm* v. *Commissioner*, 326 U. S. 287, 293 (1945).

The importance of a determination by this Court of when a corporate taxpayer's existence may be deemed to be terminated for Federal tax purposes is apparent from the number of litigated cases in lower courts which have involved the question. Moreover, as stated above, the decision of the Court of Appeals is in direct conflict with the decisions in three of those cases and contrary to the reasoning of several others.

Conclusion

For the foregoing reasons the petition for a writ of certiorari should be granted.

Respectfully submitted,

AMERICAN WELL AND PROSPECTING COMPANY

Petitioner,

by

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July 12, 1956.

APPENDIX

Statutes and Regulations Involved

Internal Revenue Code of 1939, 53 Stat., Part 1:

Sec. 710. Imposition of Tax.

. . .

(b) *Definition of Adjusted Excess Profits Net Income.*—As used in this section, the term "adjusted excess profits net income" in the case of any taxable year means the excess profits net income (as defined in section 711) minus the sum of:

(1) *Specific Exemption* . . .

(2) *Excess Profits Credit* . . . ; and

(3) *Unused Excess Profits Credit.*—The amount of the unused excess profits credit adjustment for the taxable year, computed in accordance with subsection (c).

(c) *Unused Excess Profits Credit Adjustment.*—

(1) *Computation of Unused Excess Profits Credit Adjustment.*—The unused excess profits credit adjustment for any taxable year shall be the aggregate of the unused excess profits credit carry-overs and unused excess profits credit carry-backs to such taxable year.

(2) *Definition of Unused Excess Profits Credit.*—The term "unused excess profits credit" means the excess, if any, of the excess profits credit for any taxable year beginning after December 31, 1939, over the excess profits net income for such taxable year, computed on the basis of the excess profits credit applicable to such taxable year. For such purpose the excess profits credit and the excess profits net income for any taxable year beginning in 1940 shall be computed under the law applicable to taxable years beginning in 1941. The unused excess profits credit for a taxable year of less than twelve months shall be an amount which is such part of the unused excess profits credit determined under the first sentence of this paragraph as the number of days in

the taxable year is of the number of days in the twelve months ending with the close of the taxable year. There shall be no unused excess profits credit for a taxable year beginning after December 31, 1946. . . .

(3) *Amount of Unused Excess Profits Credit Carry-Back and Carry-Over.*—

(A) *Unused Excess Profits Credit Carry-Back.*—If for any taxable year beginning after December 31, 1941, the taxpayer has an unused excess profits credit, such unused excess profits credit shall be an unused excess profits credit carry-back for each of the two preceding taxable years, except that the carry-back in the case of the first preceding taxable year shall be the excess, if any, of the amount of such unused excess profits credit over the adjusted excess profits net income for the second preceding taxable year computed for such taxable year (i) by determining the unused excess profits credit adjustment without regard to such unused excess profits credit, and (ii) without the deduction of the specific exemption provided in subsection (b) (1).

. . .

SEC. 712. EXCESS PROFITS CREDIT—ALLOWANCE.

(a) *Domestic Corporations.*—In the case of a domestic corporation which was in existence before January 1, 1940, the excess profits credit for any taxable year shall be an amount computed under section 713 or section 714, whichever amount results in the lesser tax under this subchapter for the taxable year for which the tax under this subchapter is being computed. In the case of all other domestic corporations the excess profits credit for any taxable year shall be an amount computed under section 714. For allowance of excess profits credit in case of certain reorganizations of corporations, see section 741.

Treasury Regulations 111:

Sec. 29.52-1. *Corporation returns.*— . . . A corporation having an existence during any portion of a taxable year is required to make a return. If a corporation was

not in existence throughout an annual accounting period (either calendar year or fiscal year), the corporation is required to make a return for that fractional part of a year during which it was in existence. A corporation is not in existence after it ceases business and dissolves, retaining no assets, whether or not under State law it may thereafter be treated as continuing as a corporation for certain limited purposes connected with winding up its affairs, such as for the purpose of suing and being sued. If the corporation has valuable claims for which it will bring suit during this period, it has retained assets, and it continues in existence. A corporation does not go out of existence if it is merely turned over to receivers or trustees who continue to operate it. A corporation which has received a charter, but has never perfected its organization, which has transacted no business and had no income from any source, may upon presentation of the facts to the collector be relieved from the necessity of making a return as long as it remains in an unorganized condition. In the absence of a proper showing to the collector such a corporation will be required to make a return. . . .

Treasury Regulations 112:

Sec. 35.710-3. *Unused excess profits credit adjustment.*—(a) *Unused excess profits credit.*—The unused excess profits credit for any taxable year beginning after December 31, 1939, is the excess of the excess profits credit for the taxable year over the excess profits net income, if any, for such taxable year. . . .

. . .

A corporation may have an unused excess profits credit for a taxable year beginning in 1946, which may be carried back to the two preceding taxable years, even though no excess profits tax is imposed for such taxable year. The unused excess profits credit for a taxable year beginning in 1946 is to be computed in the same manner as though an excess profits tax were imposed for such taxable year. . . . There will be no unused excess profits credit for a taxable year beginning after December 31, 1946.

EXHIBIT A

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 11,588

AMERICAN WELL AND PROSPECTING COMPANY,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

APPEAL FROM THE TAX COURT OF THE UNITED STATES

Argued October 7, 1955

Before BIGGS, *Chief Judge*, and MARIS and GOODRICH, *Circuit Judges*

OPINION OF THE COURT

(Filed March 22, 1956)

By BIGGS, *Chief Judge.*

The taxpayer, American Well and Prospecting Company, is a Texas corporation organized in 1931. It was engaged in manufacturing and selling oil well rotary drilling equipment and accessories and in the making of armaments for the United States for a number of years prior to 1946. Bethlehem Steel Corporation acquired all of the outstanding capital stock of the taxpayer in 1944 and still holds it.

On December 19, 1945, the taxpayer entered into a contract with Bethlehem Supply Company (Supply), then and now another wholly owned subsidiary of Bethlehem Steel

Corporation. Supply agreed to assume, pay and perform all of the liabilities and obligations of the taxpayer as of the opening of business on January 1, 1946, and also agreed to perform for the taxpayer all of its obligations with respect to certain contracts and leases relating to the machinery and equipment owned by the United States government. It was further agreed that, if taxpayer purchased any such equipment subsequently, it would resell the equipment to Supply at cost, unless its agreement with the United States prohibited such a course. The taxpayer agreed that it would sell to Supply all of its transferable assets, save its corporate records and franchise. Certain physical equipment owned by the United States was, of course, excluded.

The contract also provided that, as soon as possible after the closing date, Supply would pay to the taxpayer for the properties to be sold an amount equal to the aggregate net book value of the property less the aggregate book value of the liabilities and obligations of the taxpayer assumed by Supply. The taxpayer also agreed that if any of the rights or interests or any of the obligations under any of its contracts could not be assigned to Supply, the taxpayer would seek to obtain the necessary consents to permit such assignments. Under the terms of the contract the taxpayer was required to cooperate with Supply, if the necessary consents could not be obtained, to the end that the obligations of the taxpayer should "be performed in such manner that the value and benefits of the contract in question shall be preserved and shall inure directly or indirectly to the benefit of the Supply Company."

On January 2, 1946, instruments of conveyance dated December 31, 1945, were delivered by the taxpayer to Supply; and Supply assumed all liabilities and obligations of the taxpayer as of the opening of business on January 1, 1946. Among the assets owned by the taxpayer and covered by the agreement were claims against the United States. Most of these were settled in 1946. The taxpayer also had certain clean-up jobs which it was obligated to

perform for the United States. In connection with these, the taxpayer purchased from the United States material and machinery owned by the government and located on the property formerly owned by the taxpayer and sold by it to Supply pursuant to the contract. The amounts necessary to effect these purchases were furnished by Supply, and Supply received the proceeds of the sale of the material and machinery. In October 1951 the taxpayer settled a claim asserted against it by the United States in the sum of $1,300 for defective material delivered prior to January 1, 1946.

Negotiations for these settlements and the purchase of machinery and supplies, hereinbefore referred to, were conducted by persons who were officers of the taxpayer but were also officers of Supply, Bethlehem Steel Company and Bethlehem Steel Corporation. These officers did not receive any compensation from the taxpayer during 1946 and 1947 but were compensated by one or more of the other companies referred to. No entries of receipts or disbursements were made on any of the taxpayer's books in connection with the settlement or the purchases and sales referred to during the year 1946. All receipts or payments in respect thereto were received or made by Supply. A former employee of the taxpayer commenced an action in June 1946 for alleged unpaid compensation in the sum of $219,000. The taxpayer filed an answer and took other action until November 1, 1948, when the suit was dismissed following the death of the plaintiff. The expenses of the litigation were borne partly by Supply and partly by the former stockholders of the taxpayer from whom Bethlehem Steel Company had purchased the taxpayer's stock.

The net proceeds of the sale of the taxpayer's properties and assets amounted to $894,929. This amount was credited to the taxpayer in the intercompany bank account maintained by subsidiary companies of Bethlehem Steel Corporation. No formal action to dissolve the taxpayer was ever taken. In both 1946 and 1947 there were meetings

of stockholders and of the board of directors for the purpose of electing directors and officers. The balance sheets of the taxpayer as of the close of business on January 2, 1946, December 31, 1946, and December 31, 1947 were identical. The substance of these balance sheets is set out below.[1]

In 1948 the taxpayer acquired four sections of a drydock for $800,000, and in 1949 the taxpayer purchased another section. These drydock facilities represented an investment of approximately $1,500,000 at the time of the hearing before the Tax Court. The taxpayer made a business of renting the drydock.

The taxpayer did not have any excess profits net income for the taxable year 1946. It is agreed, however, that if the taxpayer is entitled to any unused excess profits credit for the year, the amount would be $74,909.27.

The Commissioner determined a deficiency in excess profits tax for the calendar year 1944 because of the disallowance of the unused excess profits credit carry-back from 1946. The Tax Court agreed with the Commissioner's determination, reasoning as follows: "The petitioner, at the beginning of 1946, disposed of the assets essential to the continued operation of the business which it had conducted with those or similar assets in 1944. Those assets were used during 1946 by Supply to carry on the business theretofore conducted by the petitioner. The results of the operation of that business during 1946 had no effect upon the petitioner but there might have been no excess profits credit to carry back to 1944 had the petitioner continued to conduct the business during 1946. Where the business was

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Assets

Accounts Receivable (intercompany bank account)	$894,929.00

Capital

Capital Stock	100,000.00
Paid-in Surplus	46,513.56
Earned Surplus	748,415.44
	$894,929.00

thus transferred to another and no longer operated by the petitioner, the latter was not intended by Congress to have the excess profits credit, wholly unnecessary for 1946, carried back to offset income of a year when the petitioner had operated the business . . . [citing cases]. It makes no difference that after several years the petitioner began to engage in a new and unrelated business." 23 T.C. 503, 507 (1954). The petition for review followed.

Section 710(c)(3)(A) of the Internal Revenue Code of 1939 governs. It provides: "If for any taxable year beginning after December 31, 1941, the taxpayer has an unused excess profits credit, such unused excess profits credit shall be an unused excess profits credit carry-back for each of the two preceding taxable years. . . ." Section 710(c)(2) states: "The term 'unused excess profits credit' means the excess, if any, of the excess profits credit for any taxable year beginning after December 31, 1939, over the excess profits net income for such taxable year, computed on the basis of the excess profits credit applicable to such taxable year. . . . There shall be no unused excess profits credit for a taxable year beginning after December 31, 1946. The unused excess profits credit for a taxable year beginning in 1946 and ending in 1947 . . . [shall be prorated to January 1, 1947]." The taxpayer's taxable year 1946 was a calendar year.

From the face of the statute, it would appear that, if the taxpayer existed as a corporation for the entire year 1946, the carry-back is mandatory. Nonetheless, the courts have held that the mere retention of a corporate shell, without internal business substance, does not entitle a corporate taxpayer to an excess profits carry-back [2] or to spread the profits of a partial year of business over the entire year, including dormant months, to reduce its excess profits tax or

2 ABC Brewing Corp. v. Commissioner, 224 F. 2d 483 (9 Cir. 1955); Wier Long Leaf Lumber Co. v. Commissioner, 173 F. 2d 549 (5 Cir. 1949) (as to the tax year 1944); Wheeler Insulated Wire Co., 22 T.C. 380 (1954); Winter & Co., 13 T.C. 108 (1949); Gorman Lumber Sales Co., 12 T.C. 1184 (1949); Rite-Way Products, Inc., 12 T.C. 475 (1949).

to create a carry-back.[3] This is the *de facto* dissolution doctrine. With few exceptions, however, the cases in which courts have applied this doctrine concerned corporations which were totally or almost completely liquidated.[4] In the case at bar, taxpayer has never been liquidated but is in fact now actively engaged in a different type of business enterprise.

Let us lay aside for the moment this factual distinction and determine whether the taxpayer would have been held to have been *de facto* dissolved in 1946 had it eventually been liquidated without acquiring any additional operating assets. For if the taxpayer would not have been held to have been *de facto* dissolved, it will be unnecessary to consider the effect of the taxpayer's subsequent drydock operations on its tax year 1946.

The test of *de facto* corporate existence is well described in Westover Co. v. Smyth, 99 F. Supp. 488 (N.D. Calif. 1951), 51-2 USTC ¶ 66,019 at page 84,075,[5] as follows: ". . . not the size of the activities but their nature and purpose; not whether some other form of business organization might have sufficed but whether the form chosen was bona fide; not whether the corporation might have dissolved earlier, but whether during the period for which it is claiming the carry-back it has engaged in corporate activities so that its existence may not be disregarded." The fact that there was no liquidating dividend in the case at bar does not preclude a finding of *de facto* dissolution. The courts have had no difficulty in holding corporations to be *de facto* dissolved when funds still remained to be distributed to stockholders.[6] Here a few entries on the Bethlehem intercompany ledgers would have reduced the taxpayer's status to a row of ciphers. Furthermore, all of the taxpayer's ac-

3 Eastern Grain Elevator Corp. v. McGowan, 95 F. Supp. 40 (W.D. N.Y. 1950); Diamond A Cattle Co., 21 T.C. 1 (1953); Winter & Co., note 2 *supra*.

4 Cases cited in notes 2 and 3 *supra*, except Wheeler and Winter.

5 The opinion of the court does not appear at 99 F. Supp. 488, but only the trial judge's findings of facts and conclusions of law and the judgment.

6 See cases cited in notes 2 and 3 *supra*, except Eastern Grain Elevator.

tivities after January 2, 1946 relating to its original enterprise were conducted merely as agent for Supply. The taxpayer incurred no costs in winding up its old business; Supply paid all the bills, including the salaries of the taxpayer's officers. The taxpayer acquired no additional income during the winding up; Supply was entitled to such income under its contract.[7] For over two years the taxpayer's balance sheet remained exactly the same as it was on January 2, 1946. In sum, the taxpayer existed only as a name through which Supply completed its acquisition of the taxpayer's former assets, and as a page in the Bethlehem intercompany ledger. There is no decision holding a corporate taxpayer entitled to an excess profits credit on such facts; there are several decisions holding corporations with considerably more business activity, whose balance sheets were affected, not entitled to the credit.[8] Thus, unless the entry into the drydock business in 1948 changes the result, the taxpayer in the case at bar would not be entitled to an excess profits credit for the tax year 1946.

The Commissioner long contended that a corporate taxpayer which changed the nature of its business was not entitled to carry back an unused excess profits credit acquired under its new enterprise to offset excess profits taxes incurred under the old enterprise. The courts uniformly

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7 In many respects, the transfer of all of the taxpayer's assets and liabilities to Supply resembled a merger. And when one corporation merges into another, its existence ceases for all excess profits tax calculation purposes. Pepsi Cola Co. v. Commissioner, 155 F. 2d 921 (2 Cir. 1946).

8 ABC Brewing Corp. v. Commissioner; Wier Long Leaf Lumber Co. v. Commissioner, both note 2 *supra*; Eastern Grain Elevator Corp. v. McGowan, note 3 *supra*; Gorman Lumber Sales Co.; Rite-Way Products, Inc., both note 2 *supra*.

Cases where courts have found sufficient business activity to entitle corporations in liquidation to excess profits credits include: Commissioner v. Allegheny Broadcasting Corp., 179 F. 2d 844 (3 Cir. 1950); Wier Long Leaf Lumber Co. v. Commissioner, note 2 *supra* (as to the tax year 1943); Brainard v. Scofield, 54-1 USTC ¶ 66,066 (W.D. Tex. 1953); Myers v. United States, 52-1 USTC ¶ 66,031 (E.D. Ark. 1952); Justice Motor Corp. v. McGowan, 97 F. Supp. 570 (W.D. N.Y. 1951); Bowman v. Glenn, 84 F. Supp. 200 (W.D. Ky. 1949), aff'd *p.c.*, 184 F. 2d 670 (6 Cir. 1950); Roeser & Pendleton, Inc., 15 T.C. 966 (1950). See also United States v. Kingman, 170 F. 2d 408 (5 Cir. 1948); Union Bus Terminal, Inc., 12 T.C. 197 (1949), aff'd *p.c.*, 179 F. 2d 399 (5 Cir. 1950).

disapproved the Commissioner's contention.[9] In those cases, however, the courts stressed the continuity of the corporate taxpayer's business activity, even though the nature of the activity changed.[10] During the years for which excess profits credits were allowed, the taxpayers involved were much more than corporate shells kept alive only for purposes of tax evasion.

In the case at bar a gap of over two years occurred between the date the taxpayer disposed of those assets necessary to carry on its old business and the acquisition of the drydock sections in 1948. During the intervening period, the taxpayer served occasionally as a funnel for Supply, which had acquired all of the taxpayer's assets and liabilities, to dispose of claims arising out of the taxpayer's former operations. The hollow quality of the taxpayer's corporate existence during this period is borne out by its balance sheets, which were identical as of the close of business on January 2, 1946, December 31, 1946, and December 31, 1947. It thus appears that after January 2, 1946, the taxpayer was little more than another corporate charter lodged in the files of the Bethlehem Steel family of corporations to await the moment when Bethlehem saw fit to breathe life into it to serve some new business purpose. In such a situation, can the drydock operations undertaken in 1948 close the hiatus of corporate inactivity during 1946, 1947, and part of 1948?

There is no case directly in point. There are, however, two Tax Court decisions involving taxpayers whose charters were similarly lodged in corporate family files. See Wheeler Insulated Wire Co., 22 T.C. 380 (1954) and Winter & Co., 13 T.C. 108 (1949). In the Wheeler case, the Sperry

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9 Mesaba-Cliffs Min. Co. v. Commisioner, 174 F. 2d 857 (6 Cir. 1949); Westover Co. v. Smyth, 99 F. Supp. 488 (N.D. Calif. 1951); Jos. Capps, Inc. v. United States, 86 F. Supp. 712 (S.D. Calif. 1949); Whitney Manufacturing Co., 14 T.C. 1217 (1950); Alprosa Watch Corp., 11 T.C. 240 (1948). Compare Aluminum Products Co. v. United States, 101 F. Supp. 373 (Ct. Cl. 1951).

10 See, *e.g.*, Westover Co. v. Smyth, note 9 *supra*, 51-2 USTC ¶ 66,019 at page 84,074; Jos. Capps, Inc. v. United States, note 9 *supra*, 86 F. Supp. at 713; Whitney Manufacturing Co., note 9 *supra*, 14 T.C. at 1221.

Corp. transferred the assets of a prosperous subsidiary, Connecticut, to another subsidiary, Wheeler, so that Wheeler's excess profits credits could be used to offset Connecticut's profits. Connecticut then attempted, unsuccessfully, to claim for its own benefit an unused excess profits credit carry-back from its assetless years to its last year of active business. It does not appear from the record in the instant case whether Supply's acquisition of the taxpayer's business assets resulted in a similar tax advantage to Supply, although we are told that the taxpayer was operating at a loss at the time of the transfer of its assets and it is probable that Supply was operating at a profit. In any event, there could be only two reasons for keeping a corporation alive under the circumstances of the case at bar in 1946: to avoid taxes, or to have a spare corporate charter conveniently ready for use whenever desired by the parent corporation. Neither is a sufficient business purpose of the taxpayer to negate the Tax Court's finding that the taxpayer in the case at bar was not entitled to an unused excess profits credit carry-back from the tax year 1946.

The decision of the Tax Court will be affirmed.

A true Copy:

Teste:

Clerk of the United States Court of Appeals for the Third Circuit.

EXHIBIT B

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

No. 11,588

AMERICAN WELL AND PROSPECTING COMPANY,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

ON PETITION TO REVIEW A DECISION OF THE TAX COURT OF THE UNITED STATES

Present: BIGGS, *Chief Judge,* and MARIS and GOODRICH, *Circuit Judges.*

JUDGMENT

This cause came on to be heard on the record from the Tax Court of the United States, and was argued by counsel.

On consideration whereof, it is now here ordered, adjudged and decreed by this Court that the decision of the said Tax Court in this cause be, and the same is hereby affirmed.

Attest:

IDA O. CRESKOFF,
Clerk

March 22, 1956

RECEIVED & FILED
MAR. 22, 1956

IDA O. CRESKOFF,
Clerk

EXHIBIT C

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

No. 11,588

AMERICAN WELL AND PROSPECTING COMPANY,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

SUR PETITION FOR REHEARING

Present: BIGGS, *Chief Judge,* and MARIS and GOODRICH, *Circuit Judges.*

After due consideration the petition for rehearing in the above-entitled case is hereby denied.

RECEIVED & FILED
APR. 18, 1956

IDA O. CRESKOFF,
Clerk

By the Court

BIGGS
Chief Judge

Dated: April 18, 1956